No. 80-189

Supreme Court, U. S.
FILED
OCT 6 1980
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

October Term, 1980

GRANT-BILLINGSLEY WHOLESALE LIQUOR CO., INC.,

Appellant,

v.

MICHAEL C. LENNEN, SECRETARY OF REVENUE FOR THE STATE OF KANSAS, *et al.*,

Appellees.

On Appeal from the Supreme Court of the State of Kansas

MOTION TO DISMISS OR AFFIRM BY APPELLEE STANDARD LIQUOR CORPORATION

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TABLE OF CONTENTS

	PAGE
Statement of the Case	2
Argument	7
A. There Is No Showing That H.B. 2020 Conflicts With the Sherman Act	7
1. Unlike the vertical price-fixing in *per se* violation of the Sherman Act found in *Midcal*, the exclusive territorial franchises mandated by H.B. 2020 require full rule-of-reason analysis	7
2. H.B. 2020 is designed to stimulate interbrand competition	10
B. The Franchise Provisions of H.B. 2020 Are Exempt from the Antitrust Laws Under the "State Action" Doctrine	19
C. The Kansas Franchise System Is a Valid Exercise of State Control Over Its Liquor Distribution System Under the Twenty-first Amendment	22
Conclusion	25

TABLE OF AUTHORITIES

PAGE

Cases:

Colby Distributing Co., Inc. v. Lennen, 227 Kan.2d 179, 606 P.2d 102 (1980) 2

California Retail Liquor Dealers Ass'n. v. Midcal Aluminum, Inc., —— U.S. ——, 100 S. Ct. 937 (1980) ..... 7, *passim*

California v. LaRue, 409 U.S. 109 (1972) 9

Capiscean Corp. v. Alcoholic Beverage Control Appeals Board, 87 Cal. App.3d 996, 151 Cal. Reptr. 492 (1979) 8

Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977) ..... 9, *passim*

Joseph E. Seagram & Sons, Inc. v. Hostetter, 384 U.S. 35 (1966) 2, 7, 9, 19

Midcal Aluminum, Inc. v. Rice, 90 Cal. App.3d 979, 153 Cal. Reptr. 757 (1979) 8

New Motor Vehicle Bd. of Cal. v. Orrin W. Fox Co., 439 U.S. 96 (1978) 21

Northern Pacific R. Co. v. United States, 356 U.S. 1 (1958) 8

Parker v. Brown, 317 U.S. 341 (1943) 18, 20

Rice v. Alcoholic Beverage Control Appeals Board, 21 Cal.3d 431, 146 Cal. Rptr. 585, 579 P.2d 476 (1978) 8

Standard Oil Co. of Cal. v. United States, 337 U.S. 293 (1949) 16

State Board v. Young's Market Co., 299 U.S. 59 (1936) 23

Tampa Electric Co. v. Nashville Coal Co., 365 U.S. 320 (1961) 16

PAGE

United States v. Arnold, Schwinn & Co., 388 U.S. 365 (1967) 8, 10
United States v. Bausch & Lomb Optical Co., 321 U.S. 707 (1944) 10
United States v. Colgate & Co., 250 U.S. 300 (1919) 10
United States v. Philadelphia National Bank, 374 U.S. 321 (1963) 16

White Motor Co. v. United States, 372 U.S. 253 (1963) 9

Statutes:

Kansas Liquor Control Act, Kan. Stat. Ann. §§41-101, *et seq.* 2
Kansas House Bill No. 2020 ..... 2, *passim*

Others:

Kansas Rules and Regulations Relating to Alcoholic Liquor, §14-4-26(a)(7) 15
Note, "*Parker* v. *Brown* Revisited," 77 Col. L. Rev. 898 (1977) 7

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On Appeal from the Supreme Court of the State of Kansas

MOTION TO DISMISS OR AFFIRM BY APPELLEE STANDARD LIQUOR CORPORATION

On the ground that the federal questions presented are so insubstantial as not to warrant further briefing or argument, appellee Standard Liquor Corporation ("Standard"), a licensed Kansas wine and spirits wholesaler and party-intervenor below, moves pursuant to Rule 16 for dismissal of this appeal or affirmance of the judgment of the Supreme Court of the State of Kansas, which sustained the constitutionality of newly enacted provisions of the Kansas liquor laws mandating exclusive territorial franchises challenged as violating the Sherman Act and, therefore, as repugnant to the Commerce and Supremacy Clauses of the federal Constitution.

Statement of the Case

This appeal is taken from the decision of the Kansas Supreme Court in *Colby Distributing Co., Inc.* v. *Lennen,* 227 Kan. 2d 179, 606 P.2d 102 (1980).[1] Finding unpersuasive a variety of claims that the new provisions were contrary to both state and federal constitutional requirements, the state court upheld the validity of the 1979 changes made in the Kansas structure for regulating alcoholic beverages[2] by Kansas House Bill No. 2020 ("H.B. 2020").

Both before and since the enactment of H.B. 2020, distillers, importers, vintners and other suppliers ("suppliers"), who are permitted in keeping with the so-called "three tier" system to sell only to licensed wholesalers, have been required to post their prices with the Department of Revenue's Division of Alcoholic Beverage Control ("ABC") and to affirm that the price of any brand and size sold to a Kansas wholesaler is as low as the lowest price charged elsewhere by that supplier.[3] Prior to H.B. 2020, the ABC Board of Review established a mandatory minimum markup percentage below which the wholesaler could not resell to the retailer. That markup was set at a level to cover all costs of doing business and to insure a profit to the wholesalers on each of the items they sold. (4a, 53a-56a) The minimum wholesaler-to-retailer price of

1. That opinion is Appendix A to appellant's Jurisdictional Statement. References to that and other appendices thereto will be by page number (*e.g.,* "4a"). References to "E——-" are to pages of the Report of the Special Committee on Liquor Laws appointed by the Kansas Legislature, which was Exhibit 4 in the trial record below and which is reprinted as an appendix hereto. References to "JS ——" are to pages of the Jurisdictional Statement.

2. See Kansas Liquor Control Act, Kan. Stat. Ann. §§41-101, *et seq.*

3. This price affirmation requirement is essentially identical to that which this Court upheld in *Joseph E. Seagram & Sons, Inc.* v. *Hostetter,* 384 U.S. 35 (1966).

every item, therefore, was fixed at a uniform level statewide. The minimum markup mandated was 15.5% on spirits and 26.5% on wines. (E4)

Under the so-called "open wholesaling" requirement of the prior regulatory structure, if a supplier elected to sell a brand to any Kansas wholesaler he also had to sell to any other distributor choosing to buy it. While no wholesaler was required to handle all brands purchased by any or all others, on those leading brands for which demand was greatest there was wasteful duplication of inventory, increased transportation expense because of smaller shipments to each wholesaler, and other higher costs to wholesalers, with resulting higher prices to consumers. (E4-E6)

During 1978, a Special Committee on Liquor Laws, set up by the Kansas Legislature, conducted hearings and consulted with the ABC concerning the "open wholesaling" requirement and the state-fixing of mandated minimum markups. The Committee heard testimony, *inter alia,* that these practices in combination forced distributors to carry nearly identical inventories, restricted competition to rivalry only on the basis of delivery service but with no promotion of individual brands, rewarded economic inefficiencies, guaranteed a profit to wholesalers, raised costs and resulted in higher prices to consumers. Because consumer prices for alcoholic beverages in neighboring states were lower than in Kansas, the Committee reported that an estimated $17 million worth of liquor was illegally purchased in 1977 by Kansans from out-of-state sources, with a resulting tax loss to the state of more than $2 million. (E3-E7)

The Committee recommended elimination of price controls at the wholesaler level and replacement of the "open wholesaling" system by exclusive territorial franchises. Under that proposal, a single wholesaler in a specified territory would represent each particular brand and re-

tailers located in that territory could buy that brand only from that franchised wholesaler. The Committee concluded that the proposed franchise system would eliminate many of the economic inefficiencies fostered under the "open" structure, would reduce the costs attributable to duplicative inventories, would bring about a more efficient distribution system, would introduce competition into the wholesale liquor industry, and would result in more equitable, lower prices for consumers. (E5-E7)

H.B. 2020 followed the Committee's study and recommendations. (5a) First, it removed the old price controls at the wholesale level. Wholesaler prices to retailers are now to be determined independently by each franchised distributor in competition with the brands of others. As the Kansas Supreme Court concluded, by thus "allowing the liquor price to seek its own level at the second tier of the liquor system, the legislature has released liquor pricing from its former status as a totally controlled commodity." (19a)

Second, no wholesaler is to sell a brand unless there is filed with the ABC a written agreement with the supplier specifying the territory within which the wholesaler is to sell that brand to retailers. No supplier is to "grant a franchise for the distribution of a brand to more than one distributor for all or part of any designated territory." (46a)

Third, with a single wholesaler thus accountable for representing a brand, broad obligations are imposed upon that franchised wholesaler to serve all retail accounts in his territory and to do so on a non-discriminatory basis with respect to both price and the supporting services which promote sale of the brand. If he fails to provide such service and pricing, the statute requires that the ABC director "shall revoke the license of such distributor." Further, in the event of any supply shortage which pre-

vents filling the orders of all retailers, apportionment plans must be approved by the director. (52a-53a)

Following enactment of H.B. 2020, three wholesalers (including appellant), dissatisfied with the brand franchises they had negotiated in the separate local markets which they served, sought a declaratory judgment and injunction in the Kansas District Court against enforcement of various provisions of the new legislation. On August 6 and 7, 1979, evidence and argument both *pro* and *con* were offered at a trial. Because Section 11 of H.B. 2020 (57a) provided a 120-day transition period and because the district court had temporarily enjoined enforcement of the new provisions, no evidence of their actual operation and effects was introduced and the trial court made no findings as to such issues of fact. Instead, without citation of judicial precedent, that court concluded on the face of the statute that its requirement of exclusive territorial franchises violated the Sherman Act.[4] (24a-39a)

The Supreme Court of Kansas stayed the trial court's determination pending appeal. In deciding the matter thereafter, the state supreme court addressed itself to the constitutionality of the new legislation primarily "on its face", because "the provisions of H.B. 2020 were not in effect on the date of trial, [thus] rendering the evidence presented highly speculative." (14a) Reversing the trial court's determination of the franchise issue, the appellate court concluded that the new provisions were a proper exercise of the state's regulatory power over liquor under the Twenty-first Amendment.

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4. The trial court also accepted the plaintiffs' argument that minimum markup percentages to be established by the ABC at the retailer-to-consumer level constituted an unlawful delegation of price-fixing authority to the wholesalers. That determination was reversed by the Kansas Supreme Court, and appellant apparently does not here appeal from that part of the decision below.

Further, however, as a separate and independent basis for upholding the provisions of H.B. 2020, the Kansas Supreme Court also found that on their face those provisions withstood the allegations of Sherman Act violation. Recognizing that "H.B. 2020 is an attempt to obtain liquor prices which are competitive with surrounding states by introducing competition into the three-tiered structure [of alcoholic beverage distribution]" and that at the distributor level H.B. 2020 "allows the price to seek its own level in the market place as a result of competition between brands" (5a), the Kansas Supreme Court concluded:

> "By allowing the liquor price to seek its own level at the second tier of the liquor system, the legislature has released liquor pricing from its former status as a totally controlled commodity. The price is no longer totally regulated, totally fixed and can now fluctuate as the competition in the market place will determine. With respect to exclusive franchising, we have noted there are now at least two distributors operating in every area of the state. Each distributes different brands, which compete with one another. Although each distributor completely controls the distribution of its brands within its territory, we find the competition among brands to be sufficient to withstand claims of restraint of trade. . . .
>
> * * *
>
> ". . . The stated legislative purpose is to introduce competition into the pricing of liquor to the public, thereby promoting the public welfare and stopping illegal liquor traffic from out of state by offering a more competitive price. There is nothing before us to show the stated purpose is not working. . . ." (19a-20a)

ARGUMENT

Appellant contends that this Court's decision in *California Retail Liquor Dealers Ass'n.* v. *Midcal Aluminum, Inc.*, —— U.S. ——, 100 S. Ct. 937 (1980), requires reversal (1) because the Kansas Supreme Court purportedly ruled that the Twenty-first Amendment permits Kansas to enact liquor legislation wholly unfettered by the Commerce Clause and federal antitrust legislation and (2) because H.B. 2020 allegedly violates the Sherman Act.

A. There Is No Showing That H.B. 2020 Conflicts With the Sherman Act.

1. Unlike the vertical price-fixing in per se violation of the Sherman Act found in Midcal, *the exclusive territorial franchises mandated by H.B. 2020 require full rule-of-reason analysis.*

To invalidate state legislation on such federal grounds, patently it must be shown at the outset that the state law is preempted because it mandates or attempts to authorize private conduct which would violate the antitrust laws and is, therefore, invalid under the Supremacy Clause.[5] That conclusion has been most recently confirmed by this Court's analysis in the *Midcal* case ("The threshold question is whether California's plan for wine pricing violates the Sherman Act"). (100 S.Ct. at 941)

Any claim that *Midcal* is controlling here as to that threshold issue must rest on a wholly superficial comparison of the two cases. In *Midcal*, this Court upheld a line of California state court decisions striking down that state's statutory delegation to private parties of the unsupervised power to set minimum resale prices to be

5. *See, e.g., Joseph E. Seagram & Sons, Inc.* v. *Hostetter*, 384 U.S. 35, 41 (1966); Note, "*Parker* v. *Brown* Revisited," 77 Col. L. Rev. 898, 899 n.7 (1977).

charged by the purchasers of their brands.[6] Such vertical price-fixing, lacking even the pretense of state review or involvement, constituted a *per se* violation of the Sherman Act on the face of the statutes and without more.

To find a state statute repugnant to the antitrust laws, *Midcal* and the California decisions it endorsed require that there must be a *per se* violation or at least, as the California Supreme Court declared, "a clear violation of the Sherman Act" mandated by the state.[7] Neither *Midcal* nor the California precedents involved state regulation of liquor distribution structure and the accountability of an exclusive distributor within a specified territory for non-discriminatory, equal access servicing of all retail accounts, regardless of their volume, distance from his warehouse, or marginal profitability owing to the high cost of serving them.

In sharp contrast, the legislation challenged here involves non-price vertical arrangements which require a full "rule-of-reason" analysis. This Court, by overruling the *per se* holding of *United States* v. *Arnold, Schwinn & Co.*, 388 U.S. 365 (1967), unequivocally re-established the proposition that vertical non-price restrictions, including exclusive territorial confinement of a distributor by a supplier, even when effected solely by private parties, require a rule-of-reason evaluation because they fail to meet the "demanding standards" for invoking the *per se* rules.[8]

6. See *Rice* v. *Alcoholic Beverage Control Appeals Board*, 21 Cal. 3d 431, 146 Cal. Rptr. 585, 579 P.2d 476 (1978); *Capiscean Corp.* v. *Alcoholic Beverage Control Appeals Board*, 87 Cal. App.3d 996, 151 Cal. Reptr. 492 (1979); *Midcal Aluminum, Inc.* v. *Rice*, 90 Cal. App. 3d 979, 153 Cal. Rptr. 757 (1979).

7. See *Rice, supra*, n.6, 579 P.2d at 482.

8. *See Northern Pacific R. Co.* v. *United States*, 356 U.S. 1, 5 (1958) ("there are certain agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use").

Continental T.V., Inc. v. *GTE Sylvania, Inc.*, 433 U.S. 36, 50 (1977). Here there has been neither opportunity nor effort in the proceedings below to assess actual competitive experience or the market effects of the franchise system at issue, particularly considering the state mandated requirement that the franchised wholesalers supply and service all retailers in their territories without discrimination in price or other competitive benefits and through rationing if necessary.

Appellant pays only grudging lip service to this Court's *Sylvania* decision, mistakenly characterizing it as having substituted the rule of reason for a *per se* approach only with respect to "the general run of non-price vertical restraints." Appellant urges the Court to use this case as the vehicle for carving out an exception to *Sylvania* and establishing a new class of *per se* violations. (JS 19-21) In *Sylvania*, however, the Court emphasized that "we do make clear that departure from the rule-of-reason standard must be based upon demonstrable economic effect. . . ."[9] (433 U.S. at 58-59) On the record below there is no demonstrable economic effect which could justify any finding of antitrust wrongdoing, let alone a *per se* violation. There was and could be no weighing of "all of the circumstances . . . in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition." (*Id.* at 49) Of necessity, therefore, the Kansas franchise provisions must be examined on their face.[10]

9. *See, also, White Motor Co.* v. *United States*, 372 U.S. 253, 263 (1963) ("We need to know more than we do about the actual impact of these arrangements on competition to decide whether they have such a 'pernicious effect on competition and lack . . . any redeeming virtues' ").

10. As the Court has stated:

> "Although it is possible that specific future applications of [the statute] may engender concrete problems of constitutional dimension, it will be time enough to consider any such problems when they arise. We deal here only with the statute on its face." *California* v. *LaRue*, 409 U.S. 109, 119 n.5 (1972), *quoting Joseph E. Seagram & Sons, Inc.* v. *Hostetter*, 384 U.S. 35, 52 (1966).

2. *H.B. 2020 is designed to stimulate interbrand competition.*

On their face, the provisions of H.B. 2020 are wholly consistent with the stimulation of interbrand competition, including price competition, among the literally hundreds of competing brands of a far larger number of suppliers which have been available in other states (by comparison with just the 260 brands of only 80 suppliers identified in trial exhibits as available in Kansas under the former "open wholesaling" system). (18a) Particularly is that true in light of the prior absence of meaningful interbrand competition in Kansas which was revealed in the report of the legislature's Special Committee. It is clear from the legislative background of H.B. 2020 that its franchise provisions, far from representing a sinister candidate for *per se* antitrust treatment, were intended to promote price and service competition previously lacking in the Kansas liquor trade.

Clearly no federal law requires that all who wish to purchase a particular product must be permitted to do so. No federal law requires that all liquor wholesalers must have access to the purchase of all brands.[11] In fact, where suppliers' products reach ultimate consumers through middlemen, this Court has declared that "the right to select . . . customers may well be the most essential factor in the maintenance of . . . service" or other competitive criteria. *United States* v. *Bausch & Lomb Optical Co.*, 321 U.S. 707, 728-29 (1944).

11. *United States* v. *Colgate & Co.*, 250 U.S. 300, 307 (1919) ("[The Sherman Act] does not restrict the long recognized right of a trader or manufacturer, engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal"); *United States* v. *Arnold, Schwinn & Co.*, 388 U.S. 365, 376 (1967) (". . . A manufacturer of a product, other and equivalent brands of which are readily available in the market, may select his customers, and for this purpose he may franchise certain dealers to whom alone he will sell his goods. . .").

In addition, in *Sylvania* the Court recognized that vertical restrictions going beyond a refusal to deal other than just with those franchised by the supplier, notwithstanding their elimination of intrabrand competition at the level of the middlemen, can enhance competition overall by achieving efficiencies and heightening the thrust of the supplier's products in interbrand competition with those of competing suppliers. The Court concluded that interbrand competition is the "primary concern of the antitrust laws" and the ultimate protection of consumers, because without it no amount of intrabrand competition can insure the availability of substitute competing products and the "significant check on the exploitation of intrabrand market power" thus provided by the existence of interbrand competition. (433 U.S. at 52 n.19)

Sylvania establishes that selective designation of wholesalers and vertical restrictions upon where and to whom they can resell, designed to maximize sales based upon the rendition of services furnished by wholesalers committed to building volume for a particular supplier's product, can be wholly consistent with the objectives of the antitrust laws. Such arrangements prevent other "free riding" wholesalers, who elect not to undertake and bear the cost of promotional, volume-building efforts, from reaping the benefits of such interbrand competitive activities performed by designated distributors obligated to maximize sales for the supplier. By reducing the volume they sell, "free riding" discourages the designated wholesalers from providing such competitive services because the costs incurred cannot be recovered.

H.B. 2020 advances the legitimate legislative purpose of orderly, efficient and competitive marketing designed to facilitate ready availability of many competing brands at all types and sizes of retail outlet in sufficient locations to insure convenient access to consumers and to encourage price competition and the provision of a variety of pro-

competitive wholesaler services. It does this by means of supplier selection of wholesalers obligated to invest their time, effort and money in furnishing all of the services necessary to promote sales of that supplier's particular brand in the most effective competition with those of other suppliers, enhancing brand recognition and consumer demand for and satisfaction with that brand.

As the trial evidence indicated, because of the importance of brand recognition in the minds of consumers, the industry deems it essential that brands be available in every outlet where they can be placed, that desirable shelf or display space be obtained at retail establishments everywhere possible, that the wholesalers educate the retailers about the brands they carry and persuade them to recommend them to consumers, that full stocks in all sizes be continually and readily available for prompt delivery to retailers wherever located, and that wholesalers provide a variety of other services, all of which are designed to build the brand and increase consumer call for it. The provision of these services is necessary not merely to realize the enhanced sales volume which results from a wholesaler's engaging in total account coverage, but also because even the few brands most heavily advertised by the suppliers cannot achieve their potential without promotional support, furnished in each local market by the wholesalers, which wins retailer and consumer acceptance of the brand and thrust for its advancement. Wholesalers protected from the "free rider" problem become willing to undertake the commitment and cost of furnishing their panoply of volume-building services not only for leading brands but also for newly introduced, less successful or even struggling brands.

Consistent with securing the broadest possible account coverage in order to achieve both maximum volume and enhance consumer awareness and demand for the brand, a wholesaler must be willing and H.B. 2020 obligates him

to serve on a non-discriminatory basis the large number of small, distant and marginal outlets which are costly to serve; he cannot concentrate solely on the large retail stores, which offer him greater profit potential but which, alone, are unable to provide the total volume for the brand which flows from marketwide availability and visibility when it is placed and featured in every possible outlet.

The existence of many retail accounts which are at best marginally profitable because of the higher costs of serving them, coupled with the lowering of the average unit costs of distributing a brand when duplication of services is avoided by placing it with one wholesaler (with resulting economies of scale), supports the adoption of the exclusive distribution established by H.B. 2020 as the lowest cost, most efficient means to introduce new brands and keep existing brands in fully effective, vigorous competition with those of other suppliers.

Appellant, however, conjectures here that a variety of anticompetitive consequences will accompany the enactment of H.B. 2020. Urging that "prices to consumers will increase to reflect the monopoly status of the surviving wholesalers," appellant cites opinion testimony by an academician that "open wholesaling" and intrabrand competition allegedly "led to lower prices" (appellant later recognizes that such competition could keep prices down only to "the lowest level permitted by law"). (JS 11, 13) Not only does the legislative history demonstrate that the high state-mandated markups sheltered costly, economically unjustifiable practices at the wholesaler level and held a guaranteed profit-protecting umbrella over even the most inefficient, but the sole record evidence[12] is that with the

12. The newspaper report cited by appellant (JS 17 n.8) is not of record. If, as appellant argues without record support, retail prices have risen since H.B. 2020, such increases could reflect increases in supplier prices to wholesalers or retailers taking higher markups even though interbrand competition could have forced wholesaler markups below the prior mandatory percentages.

advent of H.B. 2020 at least Standard, the wholesaler then accounting for the largest volume on a statewide basis, posted lower prices than the pre-existing minimum markups.

Similarly, appellant ignores the fact that suppliers in their own self-interest will seek those efficient wholesalers who, while rendering full services to all accounts, will maintain low, competitive markups. Once a supplier sets his affirmation FOB price to his wholesaler, the supplier can derive no benefit from the wholesaler's markup since any increase in price at that level goes into the wholesaler's pocket, not the supplier's. Once his price is set, the supplier's only interest is in maximizing his own profits by maximizing the volume of sales of his brands. That goal is best achieved by the lowest wholesaler markup. As this Court recognized in *Sylvania,* a supplier will select the middleman who provides the distribution and service which most effectively market his products at the lowest cost. As the Court stated:

> " 'Generally a manufacturer would prefer the lowest retail price possible, once its price to the dealers has been set, because a lower retail price means increased sales and higher manufacturer revenues.' [Citation omitted] In this context, a manufacturer is likely to view the difference between the price at which it sells to its retailers and their price to the consumer as its 'cost of distribution,' which it would prefer to minimize." (433 U.S. at 56 n.24)

The economic logic of this analysis is equally applicable to wholesaler prices to retailers.

Appellant also speculates that there is no limit to the number of suppliers and brands that "one distributor may tie up in the state" and that "interbrand competition may be reduced to a 'shadow-boxing' exercise within the sales

force of a single distributor." (JS 5) Again appellant chooses to ignore the economic self-interest of suppliers who, by any stretch of the imagination, cannot be assumed willing to countenance anything less than full "heavyweight championship" representation of any brand exclusively franchised to a wholesaler. In fact, the evidence below demonstrates that in the negotiation of franchises suppliers carefully explored what competing brands a particular wholesaler would be handling and refused to place any brand with him that was in direct, head-to-head conflict with some other supplier's brand for which he was franchised.[13] Moreover, appellant implies that the franchise agreements required by H.B. 2020, once filed, are "in perpetuity." (*e.g.*, JS 20) Apart from the fact that such agreements are made expressly subject to termination or alteration during their term for reasonable cause (47a-48a), §14-4-26(a)(7) of the Kansas Rules and Regulations Relating to Alcoholic Liquor provides that franchises may be limited to a definite period.

In support of its contention that at the wholesaler level "severe oligopolistic conditions [have been] brought about by H.B. 2020," appellant relies at length upon supposed "market share" data.[14] (JS 8-10, 15-16) Those data are

13. Appellant's own exhibits show, for example, that such substantial direct competitors and leading brands as Seagram's V.O. and Hiram Walker's Canadian Club, Somerset's Tanqueray and Kobrand's Beefeater, General Wine's Chivas Regal and Somerset's Johnny Walker Black, Paddington's J&B Rare and Buckingham's Cutty Sark, Austin Nichol's Wild Turkey and Jack Daniel's Black Label, were franchised to different wholesalers in each market area.

14. Appellant also argues that at the supplier level of the industry there is allegedly a high degree of concentration and a small number of producers dealing in heavily advertised, strongly differentiated products. Appellant concludes that such an environment is scarcely "conducive to wide-open interbrand competition, or likely to be improved by the introduction of absolute intrabrand restraints." (JS 8, 16) Neither court below made findings to support that conclusion and, even accepting the erroneous "market share" data treated above,

(footnote continued on next page)

in fact simply statewide case sales by suppliers into Kansas for the year 1978, from which appellant has calculated, brand by brand, the totals which purportedly would have been sold by the newly franchised distributors had they had franchises for those brands in that period. As such, even apart from the fact that wholesaler sales to retailers do not necessarily occur in the same year shipments are received from the supplier, obviously appellant's figures do not reflect what is happening in 1980 under the new franchise system with heightened interbrand competition, the introduction of new brands and a host of other factors neither of record nor knowable at the time of trial.

Moreover, even for the year 1978 and on the assumptions made by appellant, those state-wide figures do not allow calculation of true market share percentages. The record demonstrates without contradiction that the entire state is not a single market. To the contrary, Kansas encompasses a number of separate, local geographic markets delimited by economic considerations, including the sharply higher costs of serving retailers the more distant they are from a wholesaler's warehouse. A wholesaler operating from a warehouse in eastern Kansas simply cannot compete for accounts in western Kansas. Consequently, only those wholesalers with warehouses in the same area, generally centered in one of the larger cities, are in effective competition with each other, and the relevant geographic market must be measured in terms of those competitive realities. *See, e.g., Standard Oil Co. of Cal.* v. *United States,* 337 U.S. 293, 299 n.5 (1949); *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 357, 359 (1963); *Tampa Electric Co.* v. *Nashville Coal Co.,* 365 U.S. 320, 327

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there is no persuasive evidence of record to sustain the sweeping claims of supplier oligopoly. In any event, if such oligopoly existed in Kansas it resulted from the "open wholesaling," minimum markup system and reflected neither the absence of supplier and brand concentration in other states where franchised distribution exists nor what will follow in Kansas from the introduction of interbrand competition.

(1961). In short, market shares must be calculated in each local area of effective competition, the only relevant markets for that purpose.

Obviously, as with Standard and the Famous Companies, when a wholesaler organization operates four or five warehouses across the state and competes in each of the several local markets, its proportion of total state sales will be higher than those for wholesalers, such as the appellant, who do not. Those statewide sales percentages offer no insight into true market shares measured by the actual relevant geographic markets. Indeed, they may conceal the fact that the wholesalers operating on less than a statewide basis may have higher shares of the one or two markets in which they compete. Such statewide figures unrelated to sales in each of the actual local market areas fail to support claims of oligopoly or dominance as to any market.[15]

Moreover, the types or generic categories selected by appellant for its share calculations (straights, blends, bonds, Canadians, scotch, gin and so on) are both too expansive and too narrow for relevant market definition and share-of-market purposes. They fail to reflect (1) the existence of distinct price categories within each of the overall type categories used solely for reporting purposes

15. Even on the erroneous statewide basis, appellant's selective references to the dominance allegedly resulting for some wholesalers with franchising are misleading. For example, appellant attributes to Standard shares of several generic types in excess of 60%. (JS 10) Apart from the deficiencies of that analysis touched upon above, the 1978 statewide volumes thus attributed to Standard constituted only minor proportions of the total spirits sold into Kansas that year:

	Attributed to Standard	*Approx. % of Total Spirits*
Rum	95%	5%
Tequila	88%	1%
Blends	65%	3%
Brandy	70%	1%
Cockails	69%	2%

and the minimal competition between brands of markedly different cost (a $15 bottle of Wild Turkey has insufficient cross-elasticity to be properly included in the same market with a $5 bottle of Ten High bourbon, but they are included in the same category for state reporting purposes) and (2) the fact that competition among brands has increasingly cut across the lines of generic types as substantial numbers of consumers have come to use vodka, rum, gin, blends, Canadians and even light bourbons interchangeably for the same mixed drinks.

Finally, appellant argues that H.B. 2020 "attempts to create an absolute bar to any consideration of the market effects of privately established agreements" and is "patently invalid on its face because it excludes consideration of the very economic and other factors that the rule of reason demands be taken into account." (JS 19) The answer to this contention is twofold.

First, appellant urges that H.B. 2020 should be overturned on its face even though, consonant with this Court's analysis in *Sylvania* of the pro-competitive benefits which may result from vertical restrictions upon distributors, the interbrand competition which is the objective of the statute may in fact create a significantly improved overall competitive environment in Kansas or arguably even a competitive utopia in which the optimum benefits conceivable for retailers and consumers might be achieved.

Second, H.B. 2020 creates an absolute bar to a full rule-of-reason evaluation of the competitive effects of any exclusive franchise agreements only if, contrary to appellant's apparent position, the statute is not a proper subject for application of the "state action" doctrine of *Parker* v. *Brown,* 317 U.S. 341 (1943), or of the Twenty-first Amendment. If either or both apply, then there is no basis for any valid claim of antitrust violation, but if neither does

then antitrust actions in federal court, with a full rule-of-reason evaluation, are available to private parties and the ~~agreements. (JS 6, 16)~~ government.

Appellee submits that H.B. 2020, as the Kansas Supreme Court concluded, does not contravene, purport to authorize or mandate any violation of the Sherman Act, and there is no substantial federal question concerning its validity under that Act. Appellant in effect asks this Court to read into the state legislation a conflict with federal law when none exists. In another case involving a challenge to state liquor regulations based upon alleged Sherman Act grounds, this Court declared:

> "In this as in other areas of coincident federal and state regulations, the 'teaching of this Court's decisions . . . enjoin[s] seeking out conflicts between state and federal regulation where none clearly exists.' *Huron Cement Co.* v. *Detroit,* 362 U.S. 440, 446. We find no such clear conflict in the present case. . . . [The state regulation] imposes no irresistible economic pressure on the appellants to violate the Sherman Act in order to comply with the requirements of [the state regulation]." *Joseph E. Seagram & Sons, Inc.* v. *Hostetter,* 384 U.S. 35, 45 (1966)

That same analysis applied to H.B. 2020 should end this appeal, and there is no need for the Court to deal with other considerations which would save the statute even if an antitrust conflict were shown.

B. The Franchise Provisions of H.B. 2020 Are Exempt from the Antitrust Laws Under the "State Action" Doctrine.

Even if the exclusive territorial franchise arrangements between private parties mandated by H.B. 2020 could be found to violate the Sherman Act on the record here, the

state's participation in that system qualifies it for exemption under the "state action" doctrine of *Parker* v. *Brown*, 317 U.S. 341 (1943). There can be no dispute but that the first requisite, reiterated in *Midcal*, is satisfied, *i.e.*, "the challenged restraint [is] 'one clearly articulated and affirmatively expressed as state policy' . . . ." (100 S. Ct. at 943) Appellant, however, claims that there is no state supervision of the restraints created by the state-mandated private agreements. (JS 6, 16)

As noted, H.B. 2020 obligates each franchised wholesaler, at the risk of mandatory license revocation, to serve all retail accounts in his designated territory and to do so on a non-discriminatory basis as to both price and services, which promote sales and build volume. Concededly, in the first instance the statute leaves to those most versed in the marketing of alcoholic beverages the negotiation of the franchises, their terms and obligations, their areas and their duration. Negotiation of all of these elements, however, is subject to the pro-competitive self-interest of the supplier in maximizing his sales volume through effective competition with the brands of other suppliers.[16] Moreover, even before a franchise has run its term, it may be terminated or altered by either party upon notice to the ABC, which must then notify all affected parties of the impending termination, modification or alteration. Thereafter, without limitation to just the two parties to the franchise, the statute provides that any aggrieved supplier or distributor is entitled to a court hearing as to whether the termination, modification or territorial alteration is for reasonable cause or violates the franchise agreement. (47a-48a)

16. The Special Committee of the legislature recommended that the ABC "be empowered to review and approve all franchise agreements and also may approve or prohibit any terminations or modifications of the franchise agreement which are not made for good cause." (E6) Regulations in support of this recommendation conceivably can be formulated once this litigation is finally resolved.

In *New Motor Vehicle Bd. of Cal.* v. *Orrin W. Fox Co.*, 439 U.S. 96 (1978), the Court found antitrust immunity for a state program involving no more supervision by the state in satisfaction of the second requisite for invoking *Parker* than is established by H.B. 2020. In *Fox,* the statute required an auto manufacturer, before entering into a new franchise within the market area of an existing franchisee, to obtain state approval upon a finding of good cause (including consideration of whether the existing franchisees were providing adequate competition and convenient service for the public) following an administrative hearing if the existing franchisee protested the establishment of the new dealership. Rejecting claims of privately initiated restraint of intrabrand competition in conflict with the Sherman Act, the Court held:

> "The dispositive answer is that the Automobile Franchise Act's regulatory scheme is a system of regulation, clearly articulated and affirmatively expressed, designed to displace unfettered business freedom in the matter of the establishment and relocation of automobile dealerships. The regulation is therefore outside the reach of the antitrust laws under the 'state action' exemption.
>
> * * *
>
> "... California has not [attempted to authorize and immunize private conduct violative of the antitrust laws]. Protesting dealers who invoke in good faith their statutory right to governmental action in the form of a Board determination that there is good cause for not permitting a proposed dealership do not violate the Sherman Act, ..." (439 U.S. 109-110)

As the Court characterized *Fox* in *Midcal,* "In view of the State's active role, ... the program was not subject to the Sherman Act." (100 S. Ct. at 943).

C. The Kansas Franchise System Is a Valid Exercise of State Control Over Its Liquor Distribution System Under the Twenty-first Amendment.

The Kansas Supreme Court found H.B. 2020 to be a constitutionally permissible state regulation of alcoholic beverages under the Twenty-first Amendment. Appellant mistakenly argues that the court held that the Amendment gave the state absolute, unfettered control over liquor, wholly unrestricted by the Commerce Clause or by federal antitrust law and contrary to this Court's ruling in *Midcal.* (JS 14, 17) Not only is the Kansas court's opinion replete with statements which disprove appellant's contention,[17] but that court would hardly have bothered to decide that H.B. 2020 does not conflict with the antitrust laws if it believed that the Twenty-first Amendment completely displaces the Sherman Act where liquor is concerned.

In *Midcal,* this Court, reiterated that "the Twenty-first Amendment grants the States virtually complete control over whether to permit importation or sale of liquor *and how to structure the liquor distribution system.*"[18] (100 S. Ct. at 946) (Emphasis added) That statement is wholly consistent with the broad sweep accorded to the Twenty-first Amendment from its adoption, including the charac-

17. The state court, *inter alia,* said that liquor "has traditionally been a subject of governmental regulation at both federal and state levels" (14a); "the Twenty-first Amendment grants broad regulatory powers to a state with regard to intrastate regulation of liquor traffic . . ." (15a); ". . . the Twenty-first Amendment did not repeal the Commerce Clause . . ." (16a); and ". . . the weight of authority, both federal and state, . . . supports the broad regulatory power of a state in the area of alcoholic liquor . . ." (18a). The Twenty-first Amendment statements of the state court are wholly consistent with this Court's analysis in *Midcal.*

18. Appellant's suggestion (JS 22) that only state-owned or monopoly distribution systems are covered by the emphasized language is totally unsupported. Neither *Midcal* nor any other decision lends any support to that contention.

terization by Justice Brandeis in *State Board* v. *Young's Market Co.*, 299 U.S. 59, 63 (1936), "Can it be doubted that a State might . . . channelize desired importations by confining them to a single consignee?" While the court below correctly recognized that the federal government retains some Commerce Clause authority over liquor, structuring their liquor distribution systems has always been and continues to be a matter of "virtually complete control" by the states under the special authority granted to them by the Twenty-first Amendment. *Midcal* teaches that where competing state and federal interests are shown to exist they must be balanced and reconciled only after careful scrutiny in a "concrete case." (100 S. Ct. at 946)

In *Midcal,* the clear federal interest in price competition and the *per se* outlawing of private vertical price-fixing were confronted only by California's claimed interest in temperance and the preservation of small retailers against their larger competitors. Even in that context, however, this Court did not make an independent judgment that the asserted state interests were less substantial than the clearly defined federal policy against price-fixing. Instead, the Court looked to the findings of the California administrative agency and courts that private price-fixing did not in fact advance the asserted state interests. This Court then concluded that nothing in the record suggested the contrary. Therefore, while noting that state court findings are not binding on this Court to the extent that they undercut states rights guaranteed by the Twenty-first Amendment, consonant with established principles of deference to state court construction of state law and findings of fact, this Court concluded that it had "no basis for disagreeing with the view of the California courts that the asserted state interests are less substantial than the national policy in favor of competition." (100 S. Ct. at 946-948) Making clear that on a different record an opposite result could follow, the Court stated:

> ". . . We need not consider whether the legitimate state interests in temperance and the protection of

> small retailers ever could prevail against the undoubted federal interest in a competitive economy. The unsubstantiated state concerns put forward in this case simply are not of the same stature as the goals of the Sherman Act." (100 S. Ct. at 948)

On the record here, there is similarly no basis for this Court to disagree with the statutory construction and findings of the Kansas Supreme Court which support, rather than undercut, the state rights guaranteed by the Twenty-first Amendment. As distinguished from the California courts' rejection in *Midcal* of unsupervised vertical price-fixing by private parties on factual findings that the otherwise legitimate state interests asserted there were not advanced by higher consumer prices, here the Kansas Supreme Court has found that there is no evidence that the statutory changes effected by H.B. 2020 are not achieving their legislative purpose. That those purposes are not legitimate state police power policy objectives, even apart from the special powers over liquor granted by the Twenty-first Amendment, cannot be seriously argued. Introducing price competition at the wholesale tier as a means of lowering consumer prices, not only to achieve that salutary public interest but also to curb illegal out-of-state purchases at prices lower than those in Kansas under the pre-existing mandated minimum markups, thereby saving the state from the loss of substantial tax revenues, would be wholly valid state purposes even if a commodity other than liquor were involved. (20a-23a)

On their face, the provisions of H.B. 2020 not only fail to mandate or authorize violations of the federal antitrust laws but there is no basis for concluding that they are not reasonably related to achieving the legislative purposes. Because exclusive franchises and vertical restrictions can enhance interbrand competition by achieving scale economies and distributional efficiencies, they must be shown upon a full rule-of-reason analysis to cause an unreasonable

restraint of trade before any conclusion can be drawn that they are contrary to federal antitrust policy and interests in competition. The achievement of lower costs and vigorous interbrand competition through such restrictions, fueled by the interacting self-interests of both suppliers and franchised wholesalers in maximizing sales of their brands, are the wholly reasonable means adopted in H.B. 2020 for achieving the legislative purposes.

On this record, appellee submits that there are in fact no competing state and federal interests which require reconciliation, and H.B. 2020 is an unquestionably valid exercise of state rights under the Twenty-first Amendment.

Conclusion

For all of the reasons set forth above, appellee urges that the appeal be dismissed or, in the alternative, that the judgment of the Kansas Supreme Court be affirmed for want of a substantial federal question.

Respectfully submitted,

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APPENDIX

Report of Special Committee on Kansas Liquor Laws

To: Legislative Coordinating Council

From: Special Committee on Kansas Liquor Laws

Re: Proposal No. 16—Liquor Laws*

Under Proposal No. 16, the Special Committee on Liquor Laws was directed to conduct "a study of the laws of Kansas relating to the sale, distribution, price control, and state regulation of liquor and other alcoholic beverages."

Background

On November 2, 1948, the people of Kansas adopted an amendment to Section 10, Article 15, of the Kansas Constitution which authorized the Legislature to regulate, license, and tax the manufacture and sale of intoxicating liquors. The 1948 amendment also declared that "the open saloon shall be and is hereby forever prohibited." As a result of this amendment, the 1949 Legislature enacted the "Kansas Liquor Control Act" (K.S.A. 41-101 *et seq.*) which provides for the regulation of all phases of the manufacture, distribution, sale, possession, and consumption of alcoholic liquor. The Act is administered by the Division of Alcoholic Beverage Control of the Department of Revenue. Except for the 1965 and 1978 amendments and some relatively minor modifications which have been approved, the Liquor Control Act has remained virtually unchanged since 1949. The one major amendment to the 1949 Act took place in 1965, when the "Private Club Act" (K.S.A. 41-2601 *et seq.*) was enacted to close a loophole in the statute

* S.B. 28, S.B. 29, S.B. 30, S.B. 31, H.B. 2018, H.B. 2019, H.B. 2020 and H.B. 2021 accompany this report. Also accompanying this report are two Concurrent Resolutions recommended for introduction by the Committee.

under which numerous phony "private clubs" were established. The Private Club Act allows the consumption of liquor by the drink in licensed private clubs, which now total over 1,000 throughout the state.

The 1978 Legislature enacted another major modification to the Act through the passage of S.B. 975, the so-called "Restaurant-Club Act." This bill authorized the sale of liquor by the drink in certain bona fide restaurants. However, during the course of this study, the Kansas Supreme Court held S.B. 975 to be unconstitutional as violative of the "open saloon" prohibition of the Kansas Constitution. (*State ex rel. Schneider* v. *Kennedy,* 225 Kan. ——).

Committee Activity

In order to become familiar with the scope and operation of the Kansas liquor laws, the Committee received extensive briefings by the Director and other staff of the Division of Alcoholic Beverage Control (ABC). These briefings covered virtually all aspects of state regulation of the liquor industry and the functions and responsibilities of the ABC Division. Individuals from all segments of the liquor industry were also invited to present their views and concerns for Committee consideration. In addition to several manufacturers, a number of distributors and an even larger number of retailers appeared before the Committee. Testimony was also received from private club and tavern owners, several trade associations representing various segments of the industry, federal liquor enforcement officials, two Minnesota State Legislators, an economist, and numerous interested persons, including the former Revisor of Statutes who drafted the Liquor Control Act. Committee

staff also prepared various memoranda relevant to the study.

While a large number of conferees asserted that the Kansas liquor laws were functioning adequately to fulfill their statutory purposes, numerous minor changes were recommended to "fine tune" and modernize the statutes. (A summary of these relatively minor changes which were recommended is available from the Kansas Legislative Research Department.) The Committee thus devoted much of its deliberations to three major policy questions:

1. Should the existing "open wholesaling" provision of the Liquor Control Act be replaced by an exclusive franchise system?
2. Should the State of Kansas continue to set the minimum prices at the wholesale and retail levels and establish minimum markups at both levels?
3. Should the people of Kansas be permitted to vote on the question of repealing the "open saloon" prohibition?

Open Wholesaling. The Liquor Control Act prohibits exclusive distributorship arrangements and requires manufacturers to sell a product to all wholesalers. Wholesalers are, in turn, required to sell the product to all retailers on an equal basis. Apparently only two other states, Oklahoma and, since 1975, Minnesota, utilize an open wholesaling system. Representatives of Kansas distributors argued that the open wholesaling system curtails the illegal activities which sometimes occur in franchise states, prevents out-of-state manufacturers from exercising undue influence over Kansas distributors, and enhances the "orderly market"

which is one stated purpose of the Act. Other testimony stated that the independence of the wholesaler would be strengthened under a franchise system and illegal activities could be minimized through the adoption of mechanisms to protect the wholesaler from arbitrary acts by the manufacturer. It was also stated that open wholesaling forces all distributors to carry nearly-identical inventories and compete only on the basis of increased service: it was argued that both of these practices result in higher costs and higher consumer prices.

Minimum Pricing. Under the Liquor Control Act, the minimum sales price for liquor at the wholesale and the retail level is established by the Alcoholic Beverage Control Board of Review on the basis of statutory guidelines, which include acquisition costs, taxes and license fees, selling costs, transportation costs, reasonable expenses, and a reasonable markup or profit. The present markups permitted to wholesalers and retailers are as follows:

Product	*Wholesaler*	*Retailer*
Spirits	15½%	28½%
Cordials	17½%	36½%
Wines	26½%	45½%

Proponents of continued price maintenance by the state asserted that the provisions eliminate illegal activities which could result from intense economic pressure, curb ruthless commercial behavior by large competitors, prevent organized crime from entering the Kansas market, and support an orderly market. Proponents also argued that the liquor industry is highly regulated, not unlike some utilities, and that state regulations of this product is appropriate. Other conferees opposed to minimum pricing

stated that it contributes to higher consumer costs, rewards economic inefficiencies, and is, in effect, a guaranteed profit for established wholesalers and retailers.

"Open Saloon" Prohibition. In 1970, the voters of Kansas rejected a proposed constitutional amendment to repeal the "open saloon" prohibition by a vote of 335,094 to 346,423. Proponents of conducting another referendum on this question stated that a rational liquor by the drink provision cannot be enacted until this prohibition is removed; that sufficient changes have occurred in the state to warrant the submission of the question to the voters, who have not had the opportunity to speak on the issue since 1970; and that the amount of interest generated by voting on the "Restaurant-Club Act" indicates that a majority of the state's voters are supportive of repealing the 1948 prohibition. Opponents of submitting the question in a referendum asserted that any relaxation of the liquor laws will lead to increased use and abuse of alcoholic beverages.

Conclusions and Recommendations

Upon the basis of this study, the Committee concludes that the bulk of the Kansas liquor laws are operating adequately and in conformity with the intent of the enactments and do not require modification at this time. However, the Committee has reached the following conclusions regarding specific areas of the liquor laws:

1. *Open Wholesaling.* The open wholesaling system should be replaced with an exclusive franchise system which grants territorial protections to wholesalers and protections aganist arbitrary and illegal acts to both wholesalers and retailers. The franchise system proposed is intended to

eliminate many of the economic inefficiencies fostered under the present system; to introduce a measure of free enterprise and competition into the wholesale liquor industry while, at the same time, providing a level of continuity which will sustain an orderly market; and to result in more equitable prices for consumers while permitting reasonable profits to wholesalers and retailers. Conversion to an exclusive franchise system, with territorial and other protections, will eliminate the need for all Kansas wholesalers to carry nearly identical inventories and thus eliminate the economic inefficiency of duplicative inventories. Under the proposed franchise system, wholesalers are protected from arbitrary and illegal activities by manufacturers and retailers are protected against similar acts by wholesalers. In addition, the state will no longer establish minimum prices at the wholesale level: this will be an item for negotiation in the franchise agreements. Enforcement activities will not be hindered by the change since the Director of Alcoholic Beverage Control will be empowered to review and approve all franchise agreements and also may approve or prohibit any terminations or modifications of the franchise agreement which are not made for good cause. The Committee believes that establishment of an exclusive franchise system will bring about a more efficient and economical liquor distribution system and will also contribute to an orderly market in which consumer prices will be maintained at equitable levels. Hopefully, the prices on a number of products will be reduced under the proposed franchise system. The Committee was presented an estimate by the Division of Alcoholic Beverage Control that during 1977 Kansans illegally purchased $17 million worth of liquor from out-of-state sources, resulting in an enforce-

ment tax loss to the state of $680,000 and a gallonage tax loss of $1.5 million. If the franchise system does result in lower prices, the tax loss to the state should be reduced as fewer people will purchase out-of-state liquor illegally. The Committee recommends that Senate Bill 28, which will effect this recommendation, be enacted.

2. *Minimum Retail Prices.* The Committee recommends that the state continue to grant minimum price markups to licensed retailers. While elimination of price controls at the retail level would certainly enhance competition, the economic effects could be extremely detrimental to the present retail industry. Estimates were received that, should price controls be removed, as may as 80 percent of the present 1,200 retailers may be put out of business. While the Committee believes that there are too many retail stores in the state and that the price control system furthers economic inefficiencies, the Committee does not recommend that an upheaval on the retail level of this magnitude be created through the premature elimination of price controls. The Comimttee is recommending that a new registration fee be established as one means of limiting the number of retail outlets. The Committee believes that reduction in the number of retail liquor stores should be a topic of continued legislative interest in the future since the degree of economic efficiency at that level will remain low unless and until many of the inefficient stores are eliminated. The Legislature should also monitor the feasibility of removing retail price controls at some future time.

3. *"Open Saloon" Prohibition.* The Committee feels strongly that the time has arrived to again submit to the people of Kansas a proposed constitutional amendment to

repeal the "open saloon" prohibition. Repeal of this obsolete provision, which was very narrowly defeated in 1970, is a matter of broad statewide importance upon which the people have a right to speak, including the substantial number of young persons who have attained voting age since 1970.

In the opinion of the Committee, the "Private Club Act" is a law supported by an array of legal fictions and ingenious definitions, representative of a circumlocutious end-run around Article 15, Section 10, of the Constitution. With over 1,000 "private clubs" serving liquor by the drink across the State of Kansas, the hypocrisy, disdain, and ridicule engendered by this Act is quite understandable. The Committee received an estimate from the Department of Revenue that, of the approximately $142 million in liquor sales reported during calendar year 1977, between $19.5 million and $20.5 million worth of liquor was ultimately consumed in a private club. This estimate indicates that 13.7 percent to 14.4 percent of the liquor being consumed in Kansas passes through private clubs. With the liquor pool, the hotel exemption, the coupon books, the membership fee and waiting period, the Class A club or Class B club distinction, it is little wonder that tourist and Kansan alike are confused by the multiplicity of such requirements. Especially unfortunate is the fact that the term "open saloon" apparently encompasses jetliners traversing the skies of Kansas: countless air travelers will remember Kansas only as the place where no liquor could be served while the airplane was over the state. The Private Club Act invites abuse, begets hypocrisy and creates widescale enforcement problems.

During the course of this study voters in 45 Kansas counties, which contain nearly 75 percent of the state's

population, were permitted to vote on the "Restaurant-Club Act." Of the total votes cast, nearly 60 percent were in favor of permitting the consumption of liquor by the drink in bona fide restaurants. Although the adverse decision by the Supreme Court rendered these votes void, the number of Kansans supportive of liquor by the drink indicates that a referendum on the issue is desirable at this time.

The Committee recommends two resolutions for consideration by the 1979 Legislature: one would repeal the "open saloon" prohibition, while the other would repeal the prohibition but permit the sale of liquor by the drink only on a county option basis. The Committee has no preference between the two resolutions. However, the Committee strongly recommends that the voters of Kansas be permitted to speak on this important issue. If the proposed amendment is approved, the Legislature can then develop a rational, workable, enforceable liquor law which will be free of the infirmities and defects of the existing statute.

4. *Registration Fee.* The Committee recommends that a new registration fee of $1,000 be established for retail license applicants. As noted above, the Committee believes that there are too many (1,200 plus) liquor stores in the state. This fee is intended to discourage new liquor store license applications. Hopefully, it will serve to reduce the number of stores and thus permit greater economic efficiencies to be achieved by the remaining fewer stores. Senate Bill 29 will establish this new fee.

5. *Election Day Closings.* The Committee recommends repeal of the provision which requires retail stores, taverns,

and cereal malt beverage (3.2 beer) retailers to close on election days during the hours the polls are open. While there may have been some valid reason for this provision during the frontier days of Kansas, no case can be made to continue this obsolete provision in contemporary society. It is ironic that there is no requirement that private clubs close on election days. House Bill 2021 will effect this recommendation.

6. *Violations by Retailers.* The Committee recommends that the Director of Alcoholic Beverage Control be given the authority to levy monetary fines, up to $1,000, on retailers for violations. At present, the Director is only authorized to suspend or revoke the retailer's license. This new provision would permit the Director to use more discretion in making the punishment fit the violation. Additionally, another recommended bill will create a rebuttable presumption that, in violations involving sales to minors, the retailer knew or should have known that the person was a minor. This provision should ease the burden on some retailers who are fooled by fraudulent identification cards in the possession of mature-looking minors. Senate Bill 30 and Senate Bill 31 will effect this recommendation.

7. *Location of Retail Stores.* The Committee recommends House Bill 2019, which would permit retail liquor stores to be located in enclosed shopping malls. At present, retail stores cannot be located in such malls because K.S.A. 41-711 requires that stores not open into another business. The bill would permit stores to open into the common area of an enclosed mall but would not permit stores to have inside entrances into other businesses. Given the number of enclosed shopping malls in the state, this appears to be

an appropriate amendment at this time. House Bill 2019 would carry out this recommendation.

8. *"Sunrise-Sunset Prohibition."* The Committee recommends that the "sunrise-sunset" provision be repealed. Under this provision, wholesalers may not move alcoholic liquors from their warehouses before sunrise or after sunset. This appears to place a burden on some wholesalers, especially in the western part of the state, who must cover large delivery territories. One result of the proposed franchise bill may be to reduce the number of wholesale branch houses in the state which will result in even larger territories for some wholesalers. This change should also have no great effect on enforcement efforts. For these reasons, the Committee recommends enactment of House Bill 2020.

9. *Liquor Licensee Restriction.* The Committee recommends K.S.A. 1978 Supp. 41-311, which prohibits law enforcement officers and persons who appoint law enforcement officers from holding any liquor license, be amended. One effect of the present statute is to prevent liquor licensees from seeking election to some city offices. Evidently, the framers of this provision feared that a licensee who was also a law enforcement officer or who appointed law enforcement officers could influence the enforcement of the liquor laws to his or her own advantage. The Committee does not believe that this situation is a problem with respect to part-time law enforcement officers or city officials. The Committee recommends that the prohibition be limited only to full-time law enforcement officers. House Bill 2018 will make this modification.

10. *Payment of Gallonage Tax.* Several wholesalers expressed concern that the time schedule for payment of the liquor gallonage tax creates financial problems which result in increased expenses. Under the present law, the tax must be paid 30 days after the wholesaler receives the merchandise. Several wholesalers requested that the time period be increased by perhaps an additional 30 days. The Committee does not feel that it has the information necessary to forecast the impact of such a change, since relatively large tax revenues are involved. The Committee does recommend that the appropriate standing committees consider this problem to determine whether a less burdensome schedule could be developed without creating problem areas for the Department of Revenue.

Dec. 15, 1978

Respectfully submitted,

/s/ Frank D. Gaines
Sen. Frank D. Gaines, Chairperson
Special Committee on Kansas
Liquor Laws

Rep. Charles J. Schwartz,
Vice-Chairperson
Sen. Edward F. Reilly, Jr.
Rep. Victor W. Kearns, Jr.
Rep. John F. Sutter